

# PERAC AUDIT REPORT



## State Contributory Retirement System

JAN. 1, 2004 - DEC. 31, 2006



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# PERAC

COMMONWEALTH OF MASSACHUSETTS | PUBLIC EMPLOYEE RETIREMENT ADMINISTRATION COMMISSION

DOMENIC J. F. RUSSO, *Chairman* | A. JOSEPH DeNUCCI, *Vice Chairman*

JOSEPH E. CONNARTON, *Executive Director*

MARY ANN BRADLEY | PAUL V. DOANE | KENNETH J. DONNELLY | JAMES M. MACHADO | DONALD R. MARQUIS

March 13, 2008

The Public Employee Retirement Administration Commission has completed an examination of the State Retirement System pursuant to G.L. c. 32, § 21. The examination covered the period from January 1, 2004 to December 31, 2006. This audit was conducted in accordance with the accounting and management standards established by the Public Employee Retirement Administration Commission, in regulation 840 CMR 25.00. Additionally, all supplementary regulations approved by PERAC and on file at PERAC are listed in this report.

In our opinion the financial records are being maintained and the management functions are being performed in conformity with the standards established by the Public Employee Retirement Administration Commission, with the exception of those noted in the finding presented in this report.

In closing, I acknowledge the work of examiners James Sweeney, James Ryan, James Tivnan and Carol Niemira who conducted this examination, and express appreciation to the Board of Retirement and staff for their courtesy and cooperation.

Sincerely,



Joseph E. Connarton  
Executive Director



## EXPLANATION OF FINDING AND RECOMMENDATION

### **Annual Statement**

The Annuity Savings Fund general ledger account cannot be reconciled to the total in the membership file generated by the computerized membership database. The difference can be primarily attributed to the volume and timing of payroll information from the various reporting units at year end. PERAC requires that each Annual Statement contain a supplemental schedule that lists the balance of each member's accumulated deductions plus interest accrued. This schedule must agree with the Annuity Savings Fund Account balance carried on the general ledger. The total in the member's Annuity Savings accounts must be available and balance to the Annuity Savings Fund.

### **Recommendation:**

A more thorough reconciliation procedure is required at year end between the primary database and the Annuity Savings Fund carried in the general ledger. All variances must be resolved to ensure individual member's accounts are correct. An administrative adjustment to the COBOL computer program would most likely address most of these variances due to volume and timing. A summary page listing the accumulated totals from the individual membership records must be compiled. The summary page should be filed with the Annual Statement.

### **Administrative Observation**

The previous PERAC Audit dated November 9, 2004 made an observation concerning a COBOL computer language program. These older technologies have limited current and future available support. This antiquated software system is the primary database for the 86,000 active members who participate in the system and the 50,000 members who receive benefits from the system. The State Retirement Board has begun studying alternatives for updating the software to a current database technology. The Board is encouraged to develop a comprehensive plan for upgrading the technology. This should improve the information flow which would significantly benefit all users.

### **Board Response:**

The membership file generated by the computerized membership database list submitted in prior audits is primarily used in preparation for the Board's actuarial valuation conducted by PERAC. The database list and accompanying data is used by the Board for multiple purposes and was not designed to be an accounting document.

## EXPLANATION OF FINDINGS AND RECOMMENDATIONS (Continued)

The Board has under taken the necessary steps to implement the data and business process changes to address the finding relating to the Annuity Savings Fund and general ledger accounting. These changes include the development of a supplemental schedule to be filed with the Annual Statement commencing with calendar year 2008. The above finding centers on the timing of financial activity and accounting assumptions relating to the year-end closing. Therefore, we would suggest the PERAC audit follow up be scheduled to coincide with the year-end accounting for the 2008 Annual Statement.

### **FINAL DETERMINATION:**

***Since the only finding relates to a year end issue the PERAC audit staff will follow up in one year after the calendar year and accounting entries are completed to ensure appropriate actions have been taken regarding the finding.***

## STATEMENT OF LEDGER ASSETS AND LIABILITIES

AS OF DECEMBER 31,			
	2006	2005	2004
<b>Net Assets Available For Benefits:</b>			
Cash	\$19,329,436	\$270,142,701	\$69,306,595
PRIT Cash Fund	20,349,728	31,230,451	24,518,888
PRIT Core Fund	20,474,344,646	17,843,801,178	16,464,687,384
Accounts Receivable	7,054,649	4,629,691	6,581,078
Accounts Payable	0	(34,201)	(28,989,550)
<b>Total</b>	<u>\$20,521,078,460</u>	<u>\$18,149,769,820</u>	<u>\$16,536,104,395</u>
<b>Fund Balances:</b>			
Annuity Savings Fund	\$4,022,622,088	\$3,759,130,291	\$3,511,976,283
Annuity Reserve Fund	1,178,412,958	1,200,920,297	1,230,023,337
Pension Fund	0	0	0
Military Service Fund	62,314	65,660	71,599
Expense Fund	0	0	0
Pension Reserve Fund	15,319,981,100	13,189,653,573	11,794,033,175
<b>Total</b>	<u>\$20,521,078,460</u>	<u>\$18,149,769,820</u>	<u>\$16,536,104,395</u>

## STATEMENT OF CHANGES IN FUND BALANCES

	Annuity Savings Fund	Annuity Reserve Fund	Pension Fund	Military Service Fund	Expense Fund	Pension Reserve Fund	Total All Funds
Beginning Balance ( 2004)	\$3,343,145,450	\$1,197,166,487	\$0	\$73,153	\$0	\$10,295,901,521	\$14,836,286,611
Receipts	380,042,164	36,783,837	478,461,560	430	68,354,922	1,976,392,233	2,940,035,146
Inter Fund Transfers	(159,461,584)	155,670,658	482,053,488	(1,984)	0	(478,260,579)	0
Disbursements	(51,749,747)	(159,597,645)	(960,515,048)	0	(68,354,922)	0	(1,240,217,362)
Ending Balance (2004)	3,511,976,283	1,230,023,337	0	71,599	0	11,794,033,175	16,536,104,395
Receipts	399,465,947	36,014,364	481,210,903	458	99,024,326	1,896,263,623	2,911,979,621
Inter Fund Transfers	(102,372,423)	98,699,549	504,322,498	(6,397)	0	(500,643,226)	0
Disbursements	(49,939,516)	(163,816,952)	(985,533,401)	0	(99,024,326)	0	(1,298,314,196)
Ending Balance (2005)	3,759,130,291	1,200,920,297	0	65,660	0	13,189,653,573	18,149,769,820
Receipts	430,431,267	35,175,614	331,294,827	423	116,985,043	2,807,695,825	3,721,582,999
Inter Fund Transfers	(114,915,053)	112,089,950	680,197,169	(3,769)	0	(677,368,297)	0
Disbursements	(52,024,416)	(169,772,904)	(1,011,491,996)	0	(116,985,043)	0	(1,350,274,359)
Ending Balance (2006)	<u>\$4,022,622,088</u>	<u>\$1,178,412,958</u>	<u>\$0</u>	<u>\$62,314</u>	<u>\$0</u>	<u>\$15,319,981,100</u>	<u>\$20,521,078,460</u>

# STATEMENT OF RECEIPTS

	FOR THE PERIOD ENDING DECEMBER 31,		
	2006	2005	2004
<b>Annuity Savings Fund:</b>			
Members Deductions	\$391,532,935	\$359,225,524	\$346,873,470
Transfers from Other Systems	10,009,676	9,603,548	7,054,140
Member Make Up Payments and Re-deposits	3,014,060	4,077,890	2,950,513
Member Payments from Rollovers	4,177,911	6,428,648	4,317,812
Investment Income Credited to Member Accounts	<u>21,696,685</u>	<u>20,130,336</u>	<u>18,846,228</u>
Sub Total	<u>430,431,267</u>	<u>399,465,947</u>	<u>380,042,164</u>
<b>Annuity Reserve Fund:</b>			
Investment Income Credited to the Annuity Reserve Fund	<u>35,175,614</u>	<u>36,014,364</u>	<u>36,783,837</u>
<b>Pension Fund:</b>			
3 (8) (c) Reimbursements from Other Systems*	0	23,327,903	22,343,084
Received from Commonwealth for COLA and Survivor Benefits	0	0	0
Pension Fund Appropriation	<u>331,294,827</u>	<u>457,883,000</u>	<u>456,118,476</u>
Sub Total	<u>331,294,827</u>	<u>481,210,903</u>	<u>478,461,560</u>
<b>Military Service Fund:</b>			
Contribution Received from Municipality on Account of Military Service	0	0	0
Investment Income Credited to the Military Service Fund	<u>423</u>	<u>458</u>	<u>430</u>
Sub Total	<u>423</u>	<u>458</u>	<u>430</u>
<b>Expense Fund:</b>			
Expense Fund Appropriation	0	0	2,105,303
Investment Income Credited to the Expense Fund	<u>116,985,043</u>	<u>99,024,326</u>	<u>66,249,619</u>
Sub Total	<u>116,985,043</u>	<u>99,024,326</u>	<u>68,354,922</u>
<b>Pension Reserve Fund:</b>			
Federal Grant Reimbursement	5,760,198	5,465,366	5,123,640
Pension Reserve Appropriation	0	0	0
Interest Not Refunded	821,453	769,778	799,165
Miscellaneous Income	0	0	0
Excess Investment Income	<u>2,801,114,174</u>	<u>1,890,028,479</u>	<u>1,970,469,428</u>
Sub Total	<u>2,807,695,825</u>	<u>1,896,263,623</u>	<u>1,976,392,233</u>
<b>Total Receipts</b>	<u>\$3,721,582,999</u>	<u>\$2,911,979,621</u>	<u>\$2,940,035,146</u>

\*prior period adjustment made in 2006 for 3(8)c receipts swept to the General Fund



# STATEMENT OF DISBURSEMENTS

FOR THE PERIOD ENDING DECEMBER 31,			
	2006	2005	2004
<b>Annuity Savings Fund:</b>			
Refunds to Members	\$50,001,252	\$48,111,312	\$49,321,983
Transfers to Other Systems	<u>2,023,164</u>	<u>1,828,205</u>	<u>2,427,764</u>
Sub Total	<u>52,024,416</u>	<u>49,939,516</u>	<u>51,749,747</u>
<b>Annuity Reserve Fund:</b>			
Annuities Paid	166,744,708	160,930,287	156,315,184
Option B Refunds	<u>3,028,196</u>	<u>2,886,666</u>	<u>3,282,461</u>
Sub Total	<u>169,772,904</u>	<u>163,816,952</u>	<u>159,597,645</u>
<b>Pension Fund:</b>			
Pensions Paid:			
Regular Pension Payments	797,380,621	774,561,557	756,742,385
Survivorship Payments	49,906,882	47,147,532	44,659,230
Ordinary Disability Payments	9,109,376	9,018,637	8,666,522
Accidental Disability Payments	80,460,157	70,043,431	65,540,422
Accidental Death Payments	10,660,207	10,850,274	10,300,201
Section 101 Benefits	3,328,183	3,230,196	3,173,734
3 (8) (c) Reimbursements to Other Systems	6,235,197	6,745,117	6,301,421
State Reimbursable COLA's Paid	54,411,374	63,936,657	65,131,133
Chapter 389 Beneficiary Increase Paid	<u>0</u>	<u>0</u>	<u>0</u>
Sub Total	<u>1,011,491,996</u>	<u>985,533,401</u>	<u>960,515,048</u>
<b>Military Service Fund:</b>			
Return to Municipality for Members Who Withdrew Their Funds	<u>0</u>	<u>0</u>	<u>0</u>
<b>Expense Fund:</b>			
Board Member Stipend	0	0	0
Salaries	2,321,657	2,147,955	1,391,832
Legal Expenses	28,454	13,361	14,371
Medical Expenses	0	0	0
Travel Expenses	7,074	10,122	9,091
Administrative Expenses	693,084	880,752	553,603
Furniture and Equipment	306,317	243,215	112,184
Management Fees	98,369,110	82,482,905	52,457,266
Custodial Fees	12,015,701	10,160,522	10,459,284
Consultant Fees	0	0	0
Rent Expenses	6,600	0	0
PERAC Expenses	3,233,289	3,084,201	3,357,290
Fiduciary Insurance	<u>3,757</u>	<u>1,293</u>	<u>0</u>
Sub Total	<u>116,985,043</u>	<u>99,024,326</u>	<u>68,354,922</u>
<b>Total Disbursements</b>	<u>\$1,350,274,359</u>	<u>\$1,298,314,196</u>	<u>\$1,240,217,362</u>

# INVESTMENT INCOME

	FOR THE PERIOD ENDING DECEMBER 31,		
	2006	2005	2004
<b>Investment Income Received From:</b>			
Cash	\$0	\$0	\$0
Pooled or Mutual Funds	<u>636,954,195</u>	<u>551,139,655</u>	<u>510,215,507</u>
<b>Total Investment Income</b>	<u>636,954,195</u>	<u>551,139,655</u>	<u>510,215,507</u>
<b>Plus:</b>			
Realized Gains	1,297,383,391	1,032,800,549	1,006,818,872
Unrealized Gains	<u>1,757,684,261</u>	<u>1,732,868,720</u>	<u>1,411,587,781</u>
Sub Total	<u>3,055,067,652</u>	<u>2,765,669,269</u>	<u>2,418,406,652</u>
<b>Less:</b>			
Realized Loss	0	0	0
Unrealized Loss	<u>(717,049,908)</u>	<u>(1,271,610,961)</u>	<u>(836,272,617)</u>
Sub Total	<u>(717,049,908)</u>	<u>(1,271,610,961)</u>	<u>(836,272,617)</u>
<b>Net Investment Income</b>	<u>2,974,971,940</u>	<u>2,045,197,963</u>	<u>2,092,349,542</u>
<b>Income Required:</b>			
Annuity Savings Fund	21,696,685	20,130,336	18,846,228
Annuity Reserve Fund	35,175,614	36,014,364	36,783,837
Military Service Fund	423	458	430
Expense Fund	<u>116,985,043</u>	<u>99,024,326</u>	<u>66,249,619</u>
<b>Total Income Required</b>	<u>173,857,765</u>	<u>155,169,484</u>	<u>121,880,115</u>
Net Investment Income	<u>2,974,971,940</u>	<u>2,045,197,963</u>	<u>2,092,349,542</u>
Less: Total Income Required	<u>173,857,765</u>	<u>155,169,484</u>	<u>121,880,115</u>
<b>Excess Income To The Pension Reserve Fund</b>	<u>\$2,801,114,174</u>	<u>\$1,890,028,479</u>	<u>\$1,970,469,428</u>

# SCHEDULE OF ALLOCATION OF INVESTMENTS OWNED

(percentages by category)

AS OF DECEMBER 31, 2006			
	MARKET VALUE	PERCENTAGE OF TOTAL ASSETS	PERCENTAGE ALLOWED
Cash	\$19,329,436	0.1%	100%
PRIT Cash Fund	20,349,728	0.1%	100%
PRIT Core Fund	<u>20,474,344,646</u>	<u>99.8%</u>	100%
<b>Grand Total</b>	<u>\$20,514,023,811</u>	<u>100.0%</u>	

For the year ending December 31, 2006, the rate of return for the investments of the State Retirement System was 16.88%. For the five-year period ending December 31, 2006, the rate of return for the investments of the State Retirement System averaged 11.67%. For the twenty-two-year period ending December 31, 2006, since PERAC began evaluating the returns of the retirement systems, the rate of return on the investments of the State Retirement System was 11.33%.

## SUPPLEMENTARY INVESTMENT REGULATIONS

The State Retirement System is invested 100% in PRIT and therefore has no supplementary investment regulations.

# NOTES TO FINANCIAL STATEMENTS

## NOTE I – SUMMARY OF PLAN PROVISIONS

The plan is a contributory defined benefit plan covering all State Retirement System member unit employees deemed eligible by the retirement board.

### ADMINISTRATION

There are 106 contributory Retirement Systems for public employees in Massachusetts. Each system is governed by a retirement board, and all boards, although operating independently, are governed by Chapter 32 of the Massachusetts General Laws. This law in general provides uniform benefits, uniform contribution requirements, and a uniform accounting and funds structure for all systems.

### PARTICIPATION

Participation is mandatory for all full-time employees. Eligibility with respect to part-time, provisional, temporary, seasonal, or intermittent employment is governed by regulations promulgated by the retirement board, and approved by PERAC. Membership is optional for certain elected officials.

There are 4 classes of membership in the State Retirement System:

#### **Group 1:**

General employees, including clerical, administrative, technical, and all other employees not otherwise classified..

#### **Group 2:**

Certain specified hazardous duty positions.

#### **Group 3:**

State police officers and inspectors.

#### **Group 4:**

Police officers, firefighters, corrections officers, and other specified hazardous positions.

## NOTES TO FINANCIAL STATEMENTS (Continued)

### MEMBER CONTRIBUTIONS

Member contributions vary depending on the most recent date of membership:

Prior to 1975:	5% of regular compensation
1975 - 1983:	7% of regular compensation
1984 to 6/30/96:	8% of regular compensation
7/1/96 to present:	9% of regular compensation
7/1/96 to present:	12% of regular compensation (State Police)
1979 to present:	an additional 2% of regular compensation in excess of \$30,000.

### RATE OF INTEREST

Interest on regular deductions made after January 1, 1984 is a rate established by PERAC in consultation with the Commissioner of Banks. The rate is obtained from the average rates paid on individual savings accounts by a representative sample of at least 10 financial institutions.

### RETIREMENT AGE

The mandatory retirement age for some Group 2 and Group 4 employees is age 65. Most Group 2 and Group 4 members may remain in service after reaching age 65. Group 4 members who are employed in certain public safety positions are required to retire at age 65. There is no mandatory retirement age for employees in Group 1.

### SUPERANNUATION RETIREMENT

A member is eligible for a superannuation retirement allowance (service retirement) upon meeting the following conditions:

- completion of 20 years of service, or
- attainment of age 55 if hired prior to 1978, or if classified in Group 4, or
- attainment of age 55 with 10 years of service, if hired after 1978, and if classified in Group 1 or 2

## NOTES TO FINANCIAL STATEMENTS (Continued)

### AMOUNT OF BENEFIT

A member's annual allowance is determined by multiplying average salary by a benefit rate related to the member's age and job classification at retirement, and the resulting product by his creditable service. The amount determined by the benefit formula cannot exceed 80% of the member's highest three year average salary. For veterans as defined in G.L. c. 32, § 1, there is an additional benefit of \$15 per year for each year of creditable service, up to a maximum of \$300.

- Salary is defined as gross regular compensation.
- Average Salary is the average annual rate of regular compensation received during the 3 consecutive years that produce the highest average, or, if greater, during the last three years (whether or not consecutive) preceding retirement.
- The Benefit Rate varies with the member's retirement age, but the highest rate of 2.5% applies to Group 1 employees who retire at or after age 65, Group 2 employees who retire at or after age 60, and to Group 4 employees who retire at or after age 55. A .1% reduction is applied for each year of age under the maximum age for the member's group. For Group 2 employees who terminate from service under age 55, the benefit rate for a Group 1 employee shall be used.
- For Group 3 members, the rate is 3% for any age.

### DEFERRED VESTED BENEFIT

A participant who has completed 10 or more years of creditable service is eligible for a deferred vested retirement benefit. Elected officials and others who were hired prior to 1978 may be vested after 6 years in accordance with G.L. c. 32, § 10.

The participant's accrued benefit is payable commencing at age 55, or the completion of 20 years, or may be deferred until later at the participant's option.

## NOTES TO FINANCIAL STATEMENTS (Continued)

### WITHDRAWAL OF CONTRIBUTIONS

Member contributions may be withdrawn upon termination of employment. Employees who first become members on or after January 1, 1984, may receive only limited interest on their contributions if they voluntarily terminate their service. Those who leave service with less than 5 years receive no interest; those who leave service with greater than 5 but less than 10 years receive 50% of the interest credited.

### DISABILITY RETIREMENT

The Massachusetts Retirement Plan provides 2 types of disability retirement benefits:

#### ORDINARY DISABILITY

**Eligibility:** Non-veterans who become totally and permanently disabled by reason of a non-job related condition with at least 10 years of creditable service

Veterans with ten years of creditable service who become totally and permanently disabled by reason of a non-job related condition prior to reaching “maximum age”.

**Retirement Allowance:** Equal to the accrued superannuation retirement benefit as if the member was age 55. If the member is a veteran, the benefit is 50% of the member’s final rate of salary during the preceding 12 months, plus an annuity based upon accumulated member contributions plus credited interest. If the member is over age 55, he or she will receive not less than the superannuation allowance to which he or she is entitled.

#### ACCIDENTAL DISABILITY

**Eligibility:** Applies to members who become permanently and totally unable to perform the essential duties of the position as a result of a personal injury sustained or hazard undergone while in the performance of duties. There are no minimum age or service requirements.

**Retirement Allowance:** 72% of salary plus an annuity based on accumulated member contributions, with interest. This amount is not to



## NOTES TO FINANCIAL STATEMENTS (Continued)

exceed 100% of pay for those who became members in service after January 1, 1988 or who have not been members in service continually since that date, the amount is limited to 75% of pay. There is an additional pension of \$667.92 per year per child who is under 18 at the time of the member's retirement, with no age limitation if the child is mentally or physically incapacitated from earning. The additional pension may continue up to age 22 for any child who is a full time student at an accredited educational institution.

### ACCIDENTAL DEATH

**Eligibility:** Applies to members who die as a result of a work-related injury or if the member was retired for accidental disability and the death was the natural and proximate result of the injury or hazard undergone on account of which such member was retired.

**Allowance:** An immediate payment to a named beneficiary equal to the accumulated deductions at the time of death, plus a pension equal to 72% of current salary and payable to the surviving spouse, dependent children or the dependent parent, plus a supplement per year, per child, payable to the spouse or legal guardian until all dependent children reach age 18 or 22 if a full time student, unless mentally or physically incapacitated.

The surviving spouse of a member of a police or fire department or any corrections officer who, under specific and limited circumstances detailed in the statute, suffers an accident and is killed or sustains injuries resulting in his death, may receive a pension equal to the maximum salary for the position held by the member upon his death.

In addition, an eligible family member may receive a one time payment of \$100,000 from the State Retirement Board.

### DEATH AFTER ACCIDENTAL DISABILITY RETIREMENT

Effective November 7, 1996, Accidental Disability retirees were allowed to select Option C at retirement and provide a benefit for an eligible survivor. For Accidental Disability retirees prior to November 7, 1996, who could not select Option C, if the member's death is from a cause unrelated to the condition for which the member received accidental disability benefits, a surviving spouse will receive an annual allowance of \$6,000.

## NOTES TO FINANCIAL STATEMENTS (Continued)

### DEATH IN ACTIVE SERVICE

**Allowance:** An immediate allowance equal to that which would have been payable had the member retired and elected Option C on the day before his or her death. For death occurring prior to the member's superannuation retirement age, the age 55 benefit rate is used. The minimum annual allowance payable to the surviving spouse of a member in service who dies with at least two years of creditable service is \$3,000, provided that the member and the spouse were married for at least one year and living together on the member's date of death.

The surviving spouse of such a member in service receives an additional allowance equal to the sum of \$1,440 per year for the first child, and \$1,080 per year for each additional child until all dependent children reach age 18 or 22 if a full time student, unless mentally or physically incapacitated.

### COST OF LIVING

Chapter 17 of the Acts of 1997 provides that the first \$12,000 of a retiree's total allowance is subject to an annual cost-of-living adjustment. Each year PERAC submits to the legislature the percentage increase in the Consumer Price Index used for indexing Social Security benefits. This benefit is subject to an annual vote of the Massachusetts General Court, but cannot exceed 3.0%.

### METHODS OF PAYMENT

A member may elect to receive his or her retirement allowance in one of 3 forms of payment.

**Option A:** Total annual allowance, payable in monthly installments, commencing at retirement and terminating at the member's death.

**Option B:** A reduced annual allowance, payable in monthly installments, commencing at retirement and terminating at the death of the member, provided, however, that if the total amount of the annuity portion

## NOTES TO FINANCIAL STATEMENTS (Continued)

received by the member is less than the amount of his or her accumulated deductions, including interest, the difference or balance of his accumulated deductions will be paid in a lump sum to the retiree's beneficiary or beneficiaries of choice.

**Option C:** A reduced annual allowance, payable in monthly installments, commencing at retirement. At the death of the retired employee, 2/3 of the allowance is payable to the member's designated beneficiary (who may be the spouse, or former spouse who remains unmarried for a member whose retirement becomes effective on or after February 2, 1992, child, parent, sister, or brother of the employee) for the life of the beneficiary. For members who retired on or after January 12, 1988, if the beneficiary pre-deceases the retiree, the benefit payable increases (or "pops up") based on the factor used to determine the Option C benefit at retirement. For members who retired prior to January 12, 1988, and the beneficiary pre-deceases the retiree, the benefit payable "pops up" in the same fashion. The Option C became available to accidental disability retirees on November 7, 1996.

### ALLOCATION OF PENSION COSTS

If a member's total creditable service was partly earned by employment in more than one retirement system, the cost of the "pension portion" is allocated between the different systems pro rata based on the member's service within each retirement system.

## NOTES TO FINANCIAL STATEMENTS (Continued)

### NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

The accounting records of the System are maintained on a calendar year basis in accordance with the standards and procedures established by the Public Employee Retirement Administration Commission.

The Annuity Savings Fund is the fund in which members' contributions are deposited. Voluntary contributions, re-deposits, and transfers to and from other systems, are also accounted for in this fund. Members' contributions to the fund earn interest at a rate determined by PERAC. Interest for some members who withdraw with less than ten years of service is transferred to the Pension Reserve Fund. Upon retirement, members' contributions and interest are transferred to the Annuity Reserve Fund. Dormant account balances must be transferred to the Pension Reserve Fund after a period of ten years of inactivity.

The Annuity Reserve Fund is the fund to which a member's account is transferred upon retirement from the Annuity Savings Fund and Special Military Service Credit Fund. The annuity portion of the retirement allowance is paid from this fund. Interest is credited monthly to this fund at the rate of 3% annually on the previous month's balance.

The Special Military Service Credit Fund contains contributions and interest for members while on a military leave for service in the Armed Forces who will receive creditable service for the period of that leave.

The Expense Fund contains amounts transferred from investment income for the purposes of administering the retirement system.

The Pension Fund contains the amounts appropriated by the governmental units as established by PERAC to pay the pension portion of each retirement allowance.

The Pension Reserve Fund contains amounts appropriated by the governmental units for the purposes of funding future retirement benefits. Any profit or loss realized on the sale or maturity of any investment or on the unrealized gain of a market valued investment as of the valuation date is credited to the Pension Reserve Fund. Additionally, any investment income in excess of the amount required to credit interest to the Annuity Savings Fund, Annuity Reserve Fund, and Special Military Service Credit Fund is credited to this Reserve account.

The Investment Income Account is credited with all income derived from interest and dividends of invested funds. At year-end the interest credited to the Annuity Savings Fund, Annuity Reserve Fund, Expense Fund, and Special Military Service Credit Fund is distributed from this account and the remaining balance is transferred to the Pension Reserve Fund.

## NOTES TO FINANCIAL STATEMENTS (Continued)

### NOTE 3 - SUPPLEMENTARY MEMBERSHIP REGULATIONS

The State Retirement System submitted the following supplementary membership regulations, which were approved by PERAC on:

October 22, 2002

The Board has adopted Travel Supplemental Regulations under the provisions of G.L. c. 7, § 50 and G.L. c. 32, § 21(4). (Regulation available upon written request)

August 1, 1994

Line of Duty Death Benefits

Rules pertaining to proceedings, required forms, other required documentation, investigation, hearing, notice, decision, payment (subject to appropriation by legislature) of benefits under §100A. Beneficiary Claim Statement Form also approved.

June 28, 1993

Conduct of Hearings

Proceedings involving removal or discharge or dereliction of duty to be conducted in accordance with administrative rules of adjudicatory procedure.

December 22, 1992

Membership/Creditable Service

Persons employed over 20 hours in a regular work week to be enrolled as members; eligible employees to be enrolled at inception of employment; pro-ration of creditable service for part-time employees; higher ed employees to receive 6 months of creditable service for 1 year sabbaticals at half pay.

Buy-Back of Prior Service

Buy-back of prior non-membership service of 6 consecutive months or less that was part-time, provisional, temporary, temporary provisional or intermittent and was not immediately followed by membership service not allowed.

November 24, 1992

Spousal Notification

Retirement option of married member to be witnessed by spouse otherwise spouse to be notified.

Proof of Age

In lieu of a birth certificate board will accept naturalization papers, passport, baptismal record, high school record or affidavits from three relatives or friends.

## NOTES TO FINANCIAL STATEMENTS (Continued)

### NOTE 4 - ADMINISTRATION OF THE SYSTEM

The System is administered by a five person Board of Retirement consisting of the Treasurer and Receiver General of the Commonwealth who shall be a member ex-officio, a second member appointed by the Treasurer, a third and fourth member who shall be elected by the members in or retired from the service of such system, and a fifth member appointed by the other four board members.

Ex-officio Member: Timothy P. Cahill, Chairman

Appointed Member: Peter Koutoujian, Sr. Term Expires: 11/30/09

Elected Member: Ralph White Term Expires: 12/31/10

Elected Member: Theresa McGoldrick, Esq. Term Expires: 4/30/09

Appointed Member: Christopher Condon Term Expires: 12/31/08

The Board members are required to meet at least once a month. The Board must keep a record of all of its proceedings. The Board must annually submit to the appropriate authority an estimate of the expenses of administration and cost of operation of the system. The board must annually file a financial statement of condition for the system with the Executive Director of PERAC.

The investment of the system's funds is the responsibility of the Board. All retirement allowances must be approved by the Retirement Board and are then submitted to the PERAC Actuary for verification prior to payment. All expenses incurred by the System must be approved by at least two members of the Board.

The following retirement board members and employees are bonded by an authorized agent representing a company licensed to do business in Massachusetts as follows:

Treasurer - Custodian:	)	\$500,000 Government Crime Policy
Ex-officio Member:	)	through National Union Fire
Elected Member:	)	Insurance Company, and
Appointed Member:	)	\$1,000,000 Staff Employee
	)	Dishonesty Policy through
Staff Employee:	)	Travelers Insurance Company

## NOTES TO FINANCIAL STATEMENTS (Continued)

### NOTE 5 - ACTUARIAL VALUATION AND ASSUMPTIONS

The most recent actuarial valuation of the State Retirement System was prepared by the Public Employee Retirement Administration Commission as of January 1, 2007.

Dollars in thousands	
The actuarial liability for active members was	\$10,977,647
The actuarial liability for vested terminated members was	438,051
The actuarial liability for non-vested terminated members was	135,289
The actuarial liability for retired members was	<u>10,119,823</u>
The total actuarial liability was	21,670,810
System assets as of that date were (actuarial value)	<u>18,445,225</u>
The unfunded actuarial liability was	<u>\$3,225,585</u>
The ratio of system's assets to total actuarial liability was	85.1%
As of that date the total covered employee payroll was	\$4,391,839

The normal cost for employees on that date was 8.36% of payroll

The normal cost for the employer was 4.20% of payroll

The principal actuarial assumptions used in the valuation are as follows:

Investment Return:	8.25% per annum
Rate of Salary Increase:	Varies by group

### GASB STATEMENT NO. 25, DISCLOSURE INFORMATION AS OF JANUARY 1, 2007

Dollars in thousands

Actuarial Valuation Date	Actuarial Value of Assets ( a )	Actuarial Accrued Liability ( b )	Unfunded AAL (UAAL) ( b-a )	Funded Ratio ( a/b )	Covered Payroll ( c )	UAAL as a % of Cov. Payroll ( (b-a)/c )
1/1/2007	\$18,445,225	\$21,670,810	\$3,225,585	85.1%	\$4,391,839	73.4%
1/1/2006	\$16,638,043	\$20,406,926	\$3,768,883	81.5%	\$4,200,577	89.7%
1/1/2005	\$16,210,981	\$19,575,008	\$3,364,257	82.8%	\$3,967,067	84.8%
1/1/2004	\$15,930,753	\$18,996,053	\$3,065,300	83.9%	\$3,841,606	79.8%

## NOTES TO FINANCIAL STATEMENTS (Continued)

### NOTE 6 - MEMBERSHIP EXHIBIT

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
<b>Retirement in Past Years</b>										
Superannuation	1,508	1,481	1,692	2,224	2,342	6,458	3,775	2,476	1,717	1,849
Ordinary Disability	31	41	35	*	*	*	*	*	*	*
Accidental Disability	84	73	60	*	*	*	*	*	*	*
<b>Total Retirements</b>	1,623	1,595	1,787	2,224	2,342	6,458	3,775	2,476	1,717	1,849
Total Retirees, Beneficiaries and Survivors	44,220	43,425	43,765	44,065	44,358	49,567	51,827	51,607	51,250	51,014
Total Active Members	82,940	86,666	83,073	87,118	88,992	81,973	80,122	81,439	82,978	84,339
<b>Pension Payments</b> (thousands)										
Superannuation	\$408,834	\$404,800	\$428,544	\$458,314	\$508,824	\$610,667	\$679,004	\$756,742	\$774,562	\$797,381
Survivor/Beneficiary Payments	30,200	31,205	32,747	34,646	36,658	39,046	43,269	44,659	47,148	49,907
Ordinary Disability	8,413	8,363	8,414	8,553	8,771	8,770	8,621	8,667	9,019	9,109
Accidental Disability	41,747	44,051	46,815	49,071	54,379	56,465	60,620	65,540	70,043	80,460
Other	<u>15,083</u>	<u>35,263</u>	<u>84,558</u>	<u>125,632</u>	<u>58,907</u>	<u>94,707</u>	<u>80,357</u>	<u>84,906</u>	<u>84,762</u>	<u>74,635</u>
<b>Total Payments for Year</b>	<u>\$504,277</u>	<u>\$523,682</u>	<u>\$601,078</u>	<u>\$676,216</u>	<u>\$667,539</u>	<u>\$809,655</u>	<u>\$871,871</u>	<u>\$960,515</u>	<u>\$985,533</u>	<u>\$1,011,492</u>

\*included with Superannuation



PERAC

Five Middlesex Avenue | Suite 304

Somerville, MA | 02145

Ph: 617.666.4446 | Fax: 617.628.4002

TTY: 617.591.8917 | Web: [www.mass.gov/perac](http://www.mass.gov/perac)